

REPORT ON EXAMINATION
OF
THE FARMERS MUTUAL FIRE INSURANCE ASSOCIATION
OF COCKE COUNTY

RECEIVED

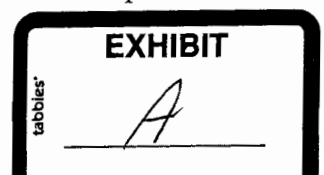
JUN 23 2004

Dept. Of Commerce & Insurance
Company Examinations

Howard Hawke
Secretary
790 Yellowsprings Rd.
Cosby, TN 37722

Examination made as of:	December 31, 2002 with Financial Statement Updated to December 31, 2003
Examiner in Charge:	Donnie Nicholson and Keith M. Patterson
Examination commenced:	January 21, 2004
Examination completed:	June 22, 2004

1



Date of Report: June 22, 2004
Examined as of : December 31, 2002 with Financial Statement
Updated to December 31, 2003
Last Examination as of : December 31, 2001

Honorable Paula A. Flowers
Commissioner
State of Tennessee
Department of Commerce and Insurance
Nashville, Tennessee 37243

Dear Commissioner:

Pursuant to your instructions, I have made an examination and submit the following report of the conditions and affairs of the

The Farmers Mutual Fire Insurance Association of Cocke County
Newport, TN

Date incorporated: 1903

Commenced Business: 1903

Officers and Directors:

<u>Title</u>	<u>Name</u>	<u>Address</u>	<u>Term Expires</u>
President	Charles Coble, Jr.	Parrottsville, TN	2003
Vice President	Carl Sisk	Cosby, TN	2003
Secretary/Treasurer	Howard Hawke	Cosby, TN	2003
Director	Charles Coble, Jr.	Parrottsville, TN	2003
Director	Carl Sisk	Cosby, TN	2004
Director	Howard Hawke	Cosby, TN	2003
Director	Floyd Strange, Jr.	Cosby, TN	2004
Director	William Miller	Newport, TN	2004
Director	Glen Ottinger	Newport	2003
Director	Geneva Raines	Cosby TN	2003
Director	Earl Daniels	Cosby, TN	2004

Compensation of officers, directors, appraisers, adjusters, et al:

President – \$1,500.00 annually plus Directors compensation
Vice President – \$0.00 annually plus Directors compensation
Secretary/Treasurer – \$5,000.00 annually plus Directors compensation
Directors Compensation - \$25.00 per meeting

Appraisals/Inspections - \$25.00 per trip for directors (\$0.00 for president and secretary)

Part-time clerical assistant - \$7.50 per hour

Agent commission- 100% of first 6 month premium per new policy written
(secretary/treasurer is the only agent)

By-Laws state "The application, when so taken by an agent, shall be approved by the resident Director and immediately transmitted to the Secretary/Treasurer; if approved by the President, the contract of insurance then be written as herein provided."

Report of changes in the Constitution of By-Laws, policy forms, or other agreements during the period covered by this examination:

None

The policy form is the same as that in effect at the last prior examination and contains a copy of the by-laws.

If copies of changes have not been filed with "The Department of Commerce and Insurance", are they filed with the workpapers of this report?

N/A

Report on reinsurance assumed and/or ceded:

Ceded:

1. Type: Excess of Loss
 Reinsurer: Hamblen Mutual Insurance Company
 Term: Continuous contract, effective August 15, 2001.
 Premium: 50% of the premium collected on each risk less the commissions paid to agents, payable semi-annually based on mutual agreement of both parties. Written contract calls for "that portion of the premium collected on each risk".

 Commission: 30% of ceded premium
 Coverage: Covers 100% of \$30,000 excess \$10,000 per risk

A "Risk" as defined shall mean a building and its contents or all buildings, including their contents, which are located within a radius of 100 feet.

The intent of both parties has been to interpret the above contract as a continuous contract; however, Article I of the agreement states a termination date of July 31, 2002. Premiums have been paid and accepted by the Reinsurer for the 2002 and 2003 policy years.

Hamblen Mutual Insurance Company is a "Tennessee County Mutual" which qualifies as an authorized reinsurer. The contract does not require approval pursuant to Tenn. Code Ann.

Appraisal and classification of risks taken:

Policies are typically written for up to 2/3 of the value of the property insured subject to policy limits of \$20,000 per structure (not including contents) and \$12,000 for other than structures. The agent performs the appraisal on the property prior to issuance of a policy. Property eligible to be insured includes dwellings (and all household goods), barns (equipment, tobacco, hay, etc.), cribs, cattle, mules, horses, farming utensils (tractors, binders, reapers, mowers, gearing, plows, harrows, saddles, buggies, wagons, and things usually stored in barns and houses).

With reinsurance available from Hamblen Mutual Insurance Company for \$30,000 excess of \$10,000 per risk, the Company can write up to \$40,000 per risk and comply with Tenn. Code Ann. § 56-22-106.

Annual rate of assessment per \$1,000 for period covered:

	<u>2002</u>	<u>2003</u>
All Lines	\$12.00	\$12.00

Assessment rates are not required to be approved by "The Department of Commerce and Insurance".

Rate of membership, policy and initial fees charged:

As of December 31, 2001, the Company had 260 policies issued and in force based on the Examination Report as of December 31, 2001. There are no initial fees or policy charges other than the \$6.00 assessment premium per \$1,000 of coverage which is charged on a semi annual basis (\$12.00 per year). The hand

written records of the Company did not give a policy count or in force total for December 31, 2002.

As of December 31, 2003, the Company had 239 policies issued and in force. This number was derived by the calculation of the examination team by entering each active policy number, in force amount and premium from the handwritten company ledger into an excel spreadsheet. The assessment rates remain unchanged for the 2003 year.

Date of last assessment:

The Company makes advance assessments of its members in January and July of each year; therefore, assessments were made on January 1, 2002; July 1, 2002; January 1, 2003; and July 1, 2003.

Amount delinquent:

\$0.00

The Company cancels policies if assessments are not paid within thirty days of due date.

Did that assessment provide for all losses, expenses and other liabilities, including borrowed money?

Yes

Amount of money borrowed since date of last statement:

None

Location of Books and Records

790 Yellowsprings Rd.
Cosby, TN 37722

Exhibit of Risks

Review of the 2002 annual statement indicated that the Company had written

premium before cancellations of \$42,419.60 while only \$254,517.60 of in force business was exhibited. This was clearly reported in error. In force of \$3,801,225 as stated in the 2001 Examination Report would indicate yearly expected premium of \$45,614.70 based on the assessment rate of \$12.00 per thousand per year.

Based on review of the above numbers and fact that all company records are handwritten, it was determined to audit the in force ledger as of December 31, 2003 and enter seriatim by policy into an excel spreadsheet.

	<u>Number</u>	<u>Amount</u>
1. In force, December 31, 2001 per exam	260	\$3,801,225
2. Written	Uncalculated	Uncalculated
3. Total	Uncalculated	Uncalculated
4. Deduct those expired and marked off	Uncalculated	Uncalculated
5. In force, December 31, 2003 per exam	239	\$3,789,525

Financial Statement (December 31, 2002)

There follows a statement of assets, liabilities and statement of income at December 31, 2002, as extrapolated from the Company's Annual Statement and the Reinsurance Bordereaux (prepared on a cash basis):

Income

Gross Assessments (per annual statement)	\$42,419.60	
Deduct Reinsurance (per reinsurance bordereaux)	20,157.30	
Deduct Return Assessments (includes back year adjustments)	0.00	
Net Assessments		\$22,262.30
Interest Income		0.00
Reinsurance Commission (30%) (per reinsurance bordereaux)		<u>6,047.20</u>
Total Income		28,309.50
Ledger Assets, December 31, 2001 (confirmed with bank)		<u>60,640.46</u>
Total Income and Balance		\$88,949.96

Disbursements

Gross amount paid policyholders for losses	\$20,110.42	
Deduct salvage and reinsurance	0.00	
Net amount paid policyholders for losses		\$20,110.42
Commission or brokerage, including membership fees retained by agents		0.00
Salaries and compensation of officers, directors, trustees and employees		6,975.00
Advertising, printing and stationary		118.80
Postage, telegrams, telephones and express		376.84
Rents		200.00
Insurance department licenses and fees		15.00
All other licenses, fees and taxes		0.00
Other disbursements		<u>100.00</u>
Total Disbursements		27,896.06
Balance "DOES NOT BALANCE TO CONFIRMED CASH PER EXAM"		<u>\$61,053.90</u>

Fire losses paid	\$18,150.00
Tornado losses paid	1,534.42
Lightning losses paid	426.00

Assets

Cash in banks (confirmed with bank)	\$67,425.51	
Total ledger assets		\$67,425.51

Non-Ledger Assets

None	\$0.00	
Gross assets		\$67,425.51

Assets Not Admitted

None	\$0.00	
Total admitted assets		\$67,425.51

Liabilities

None	\$0.00	
Total liabilities		<u>\$0.00</u>
Surplus over liabilities		\$67,425.51

Total		<u>\$67,425.51</u>
-------	--	--------------------

List of Bank Deposits:

<u>Name</u>	<u>Amount on Bank Statement</u>	<u>Balance per Examination</u>
National Bank of Tennessee	\$16,873.01 (dda)	\$16,873.01
National Bank of Tennessee	\$10,552.50 (savings)	\$10,552.50
US Bank	\$40,000.00 (C.D.)	\$40,000.00

Notes to December 31, 2002 Financial Statement:

It is apparent from the review of the above numbers that the annual statement is incomplete. No cancellations are exhibited and the gross assessments are incorrect due to the fact that more cash is in the bank than would be possible based on the collected and deposited premium based on the Company annual statement calculations. These factors contributed to the need for the detail review of the Company's in force policy and premium registers. The 2003 Financial Statement as audited per examination follows.

Financial Statement (December 31, 2003)

There follows a statement of assets, liabilities and statement of income at December 31, 2003, as established by this examination:

Income

Gross Assessments (per Company expected premium listing)	\$47,581.40	
Deduct Reinsurance	21,957.90	
Deduct Return Assessments (includes back year adjustments)	4,149.42	
Net Assessments		\$21,474.08
Interest Income (includes 2 years of C.D. interest)		3,575.52
Reinsurance Commission (30%)		<u>6,587.38</u>
Total Income		31,636.98
 Ledger Assets, December 31, 2002 (confirmed with bank)		<u>67,425.51</u>
Total Income and Balance		\$99,062.49

Disbursements

Gross amount paid policyholders for losses	\$5,894.18	
Deduct salvage and reinsurance	0.00	
Net amount paid policyholders for losses		\$5,894.18
Commission or brokerage, including membership fees retained by agents		1,758.00
Salaries and compensation of officers, directors, trustees and employees		7,674.00
Advertising, printing and stationary		6.00
Postage, telegrams, telephones and express		836.13
Rents		200.00
Insurance department licenses and fees		15.00
All other licenses, fees and taxes		1,693.66
Other disbursements		<u>149.99</u>
Total Disbursements		18,226.96
 Balance		<u>\$80,835.53</u>

Fire losses paid	\$2,957.23
Tornado losses paid	2,011.95
Lightning losses paid	925.00

Assets

Cash in banks (confirmed with bank)	\$80,835.53	
Total ledger assets		\$80,835.53

Non-Ledger Assets

None	\$0.00	
Gross assets		\$80,835.53

Assets Not Admitted

None	\$0.00	
Total admitted assets		\$80,835.53

Liabilities

None	\$0.00	
Total liabilities		<u>\$0.00</u>
Surplus over liabilities		\$80,835.53

Total		<u>\$80,835.53</u>
-------	--	--------------------

List of Bank Deposits:

<u>Name</u>	<u>Amount on Bank Statement</u>	<u>Balance per Examination</u>
National Bank of Tennessee	\$26,707.76 (dda)	\$26,707.76
National Bank of Tennessee	\$54,127.77 (savings)	\$54,127.77

Description of other assets:

None

Assets pledged or hypothecated:

None

Comments on claims, borrowed money and other liabilities:

There were paid claims totaling \$20,110.42 for the 2002 year and only \$5,894.18 of paid claims for the 2003 year. Claims appear to be paid in accordance with policy provisions and settlements were made promptly upon receipt of proper evidence of the Company's liability.

Comments on acts of officers and directors; any apparent violations of the Association's By-Laws, or of the laws of the State of Tennessee; general comments regarding the conduct of business:

The Company has been examined as of December 31, 2000; 2001; and now 2002 due to the fact that the information exhibited on their annual statements filed with "The Department of Commerce and Insurance" did not balance to the calculation format required. All records relating to the operation of the Company are handwritten documents which additionally makes it more difficult to audit the data. The current situation has required that examiners from "The Department of Commerce and Insurance" physically inspect the Company's records each year to determine the Company's financial position.

The Secretary/Treasurer of the Company has indicated that he intends to resign his office effective with the end of the fiscal year which ends July 31, 2004. Discussions are currently underway with the manager of Hamblen Mutual Insurance Company in the expectation that the personnel who maintain the books and records of Hamblen Mutual would maintain the books and records of the Company. If this agreement is approved by the membership of the Company at its annual meeting in August 2004, the premium records and in force listing could be computerized which would enable cross checks of financial data and effect better controls. Hamblen Mutual already maintains a listing of claim filings as part of their reinsurance agreement with the Company.

The computerization of records and premium collections will also allow calculation of the reinsurance premium as stated in the reinsurance agreement. Presently, the two companies have agreed to a premium of 50% of the premium collected on each risk less the commissions paid to agents, payable semi-annually. The written contract calls for "that portion of the premium collected on each risk".

The reinsurance agreement between the Company and Hamblen Mutual has been extended each year under the same terms by mutual agreement of the two companies; however, no written documentation of this intent has been effected. The signed agreement has a termination date of July 31, 2002.

Recommendations:

In order for the annual statement filings to be correct, it is recommended that the Company computerize their record keeping system or obtain audit services from a qualified accounting firm or individual.

The Company and Hamblen Mutual Insurance Company should either amend the current agreement to where it is continuous until cancelled or affect a new written agreement extending the reinsurance agreement each year to show a current termination date.

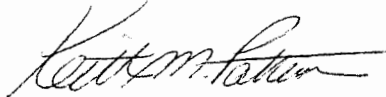
Conclusion

It was determined that, as of December 31, 2002, the Company had admitted assets of \$67,425.51 and liabilities, exclusive of capital, of \$0.00. Thus, there existed for the additional protection of the policyholders, the amount of \$67,425.51 in the form of unassigned funds (surplus).

After updating the financial data to December 31, 2003, it was determined that, as of December 31, 2003, the Company had admitted assets of \$80,835.53 and liabilities, exclusive of capital, of \$0.00. Thus, there existed for the additional protection of the policyholders, the amount of \$80,835.53 in the form of unassigned funds (surplus).

The courteous cooperation of Howard Hawke, Secretary/Treasurer extended during the course of the examination is hereby acknowledged.

Respectfully submitted,



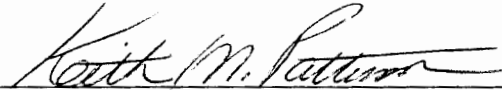
Keith M. Patterson
Insurance Examiner
State of Tennessee



Donnie Nicholson
Insurance Examiner
State of Tennessee

Affidavit

The undersigned deposes and says that he has duly executed the attached examination report of The Farmers Mutual Fire Insurance Association of Cocke County dated June 22, 2004, and made as of December 31, 2002, with Financial Statement Updated to December 31, 2003 on behalf of the Tennessee Department of Commerce and Insurance. Deponent further says he is familiar with such instrument and the contents thereof, and that the facts therein set forth are true to the best of his knowledge, information and belief.



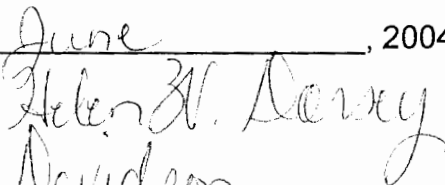
Keith M. Patterson
Insurance Examiner
State of Tennessee
Southeastern Zone, NAIC

Subscribed and sworn to before me

this 22nd day of

June, 2004

Notary



County

Davidson

State

Tennessee

Commission Expires

03/25/06